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No. 94-_____

IN THE
SUPREME COURT OF THE UNITED STATES
October Term, 1994

WEST VIRGINIA STATE DEPARTMENT OF TAX AND REVENUE,
Petitioner,

v.

INTERNAL REVENUE SERVICE,
Respondent.

Petition for Certiorari to the United States Court of Appeals for the Third Circuit

---

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether a property tax is "incurred," for purposes of determining whether it is an "administrative expense" under Section 503 of the Bankruptcy Code, when it is assessed.

THE PARTIES

Petitioner is the West Virginia State Department of Tax and Revenue.

Respondent is the Internal Revenue Service of the United States of America.

Other interested parties: These proceedings involve the bankruptcy of Columbia Gas Transmission Corporation and Columbia Gas Systems, Inc., and thus those corporations are necessarily interested in the outcome of this case.

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IN THE
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---

PETITION FOR WRIT OF CERTIORARI

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Third Circuit is officially reported at 37 F.3d 982 (3d Cir. 1994), and is reprinted in Appendix B. The denial of petitioner's petition for rehearing in banc is reprinted in Appendix A. The ruling of the United States District Court for the District of Delaware is not officially reported, but is reprinted in Appendix C. The ruling of the United States Bankruptcy Court for the District of Delaware is officially reported at 146 B.R. 114 (Bankr. D. Del. 1992), and is reprinted in Appendix D.

STATEMENT OF JURISDICTION

The United States Court of Appeals for the Third Circuit entered the decision appealed from in this case on October 5, 1994. Petitioner filed a petition for rehearing en banc on October 18, 1994, which was denied on October 28, 1994. This Court has jurisdiction to review this case pursuant to 28 U.S.C. § 1254(l). The United States Bankruptcy Court for the District of Delaware had jurisdiction of this case in the first instance pursuant to 28 U.S.C. § 1471 because the issues before the court concerned construction of the United States Bankruptcy Code.

STATUTES INVOLVED

11 U.S.C. § 503(b)(1)(B)(i) provides:

§ 503

. . .

(b) After notice and a hearing, there shall be allowed, administrative expenses, other than claims allowed under section 502(f) of this title, including --

(1) . . .

(B) any tax --

(i) incurred by the estate, except a tax of a kind specified in section 507(a)(7) of this title

11 U.S.C. § 507(a) provides:

§ 507 Priorities.

(a) The following expenses and claims have priority in the following order:

(1) First, administrative expenses allowed under section 503(b) of this title. . . .

. . . .

> (7) Seventh, allowed unsecured claims of governmental units, only to the extent that such claims are for --
>
> . . . .
>
> (B) a property tax assessed before the commencement of the case and last payable without penalty after one year before the date of the filing of the petition.

Pertinent portions of the following sections of the West Virginia Code are reprinted in Appendix F:

W. Va. Code § 11-6-1
W. Va. Code § 11-6-9
W. Va. Code § 11-6-11
W. Va. Code § 11-6-13
W. Va. Code § 11-6-14
W. Va. Code § 11-6-16
W. Va. Code § 11-6-18
W. Va. Code § 11-6-23
W. Va. Code § 11-8-8
W. Va. Code § 11-8-9
W. Va. Code § 11-8-10
W. Va. Code § 11-8-12
W. Va. Code § 11-8-14

STATEMENT OF THE CASE

This case involves the priority status in bankruptcy of approximately 6.7 million dollars in 1992 property taxes owed to the State of West Virginia by the debtor-in-possession, Columbia Gas Transmission Corporation (hereafter "Debtor"). The priority status accorded this tax debt depends on whether it was "incurred," within the meaning of 11 U.S.C. § 503(b)(1)(B)(i), before or after July 31, 1991, the date on which the Debtor filed its Chapter 11 petition in bankruptcy.

The property taxes at issue were levied in 1992 upon the assessed value of property held by the Debtor as of December 31, 1990 - the "status date."[1] The assessment was issued October 31, 1991, by the West Virginia Board of Public Works ("BPW") based on property reported by the taxpayer on an information return. (Appendix E, ¶ 8). A lien for the 1992 taxes did not arise until December 31, 1991, and the first payment on the taxes was not due until September of 1992. (Appendix E, ¶¶ 9 and 10). The assessment of the Debtor's property, the levy of the tax rate upon that assessed value, the attachment of the lien, the preparation of tax invoices, and the date on which the tax was due and payable *all* occurred *after* the Debtor filed its petition in bankruptcy.[2]

On February 14, 1992, the Debtor filed a Motion for Authorization to Pay Certain Property Tax Liabilities, which property tax liabilities included the 1992 West Virginia property taxes at issue in this case. (Appendix E, ¶ 1). The Internal Revenue Service was the only party to object to the Debtor's Motion, maintaining that the taxes were "incurred"

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[1]*See* Stipulation of Facts executed by Debtor, the IRS, and the State of West Virginia and submitted to the Bankruptcy Court ("Stipulation"), ¶¶ 3 and 5, Appendix E.

[2]The calculation and payment of public utility taxes in West Virginia includes events that span a four year period. December 31 of the first year is the "status date," with reference to which date the BPW determines the ownership and value of property in the state. W. Va. Code 11-6-1. The year following the status date is the "assessment year," during which the taxpayer files its return listing property it owns in the state as of the status date and the BPW appraises the property, then calculates and issues its assessed value of the taxpayer's property. W. Va. Code §§ 11-6-1, 11-6-11. A lien attaches on December 31 of the assessment year. W. Va. Code § 11-6-23. The year following the assessment year is the "tax year," (1992 in this case) during which the taxes are levied by the State and local levying bodies, and during which the first half installment of tax is due. W. Va. Code §§ 11-6-18, 11-8-8, 11-8-9, 11-8-10, 11-8-12, and 11-8-14. The last half installment is due in March of year four.

on the "status date." The Debtor and West Virginia contended that the 1992 property taxes were entitled to priority as administrative expenses because they were assessed and levied (and therefore "incurred") post-petition.

The United States Bankruptcy Court for the District of Delaware denied the Debtor's Motion, ruling that the 1992 property taxes were "incurred by [Debtor] prior to the filing of its petition." (Appendix D, p. 8). West Virginia and the Debtor appealed to the United States District Court for the District of Delaware, and then to the United States Court of Appeals for the Third Circuit, which courts affirmed the decision of the bankruptcy court. (Appendices B and C). West Virginia is asking that certiorari be granted to review the opinion and order of the Third Circuit.

The lower courts in this case have interpreted Sections 503 and 507 of the Bankruptcy Code in such a way as to create a gap in what should be a seamless transition from seventh priority to first priority status for property taxes. The lower courts' decisions have significantly undermined the congressional policy favoring tax-creditors in bankruptcy proceedings. This policy is of great importance to the financial stability of all state and local governments. *See Bull v. U.S.*, 295 U.S. 247, 259, 55 S. Ct. 695, 79 L.Ed. 1421 (1935) ("taxes are the lifeblood of government and their prompt and certain availability an imperious need").

The result of the decisions of the courts below is that the Debtor's 1992 West Virginia property taxes, which are unsecured, are denied any priority in bankruptcy. This result is inconsistent with Section 507(a)(7)(B) of the Bankruptcy Code, which determines the priority of *pre*-petition property taxes according to when they were "assessed." The construction of the Bankruptcy Code by the lower courts creates an anomaly whereby property taxes which were assessed *earlier* than the taxes at issue received a seventh priority status, and taxes which were assessed *later* than those at issue are given first priority as administrative expense. Thus, taxes assessed both before *and* after the

taxes at issue enjoy priority, while those at issue here receive no priority. Indeed, according to the reasoning of the decisions below, the estate was not permitted to treat its annual property tax liability as an administrative expense until September, 1993, over two years after the bankruptcy petition was filed.

This anomalous result does not obtain if Sections 503 and 507 of the Bankruptcy Code are read in *pari materia* so that property taxes are considered "incurred," under both Sections, when those taxes are assessed.

REASONS FOR GRANTING THE WRIT

I. THE THIRD CIRCUIT'S INTERPRETATION OF SECTIONS 503 AND 507 OF THE BANKRUPTCY CODE WRONGLY DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW.

A. The Third Circuit's Decision Creates An Internal Inconsistency In The Bankruptcy Code.

Section 503(b)(1)(B)(i) of the Bankruptcy Code provides that "any tax incurred by the estate, except a tax of a kind specified in Section 507(a)(7)" is an administrative expense and entitled to a first priority.[3] Although the Bankruptcy

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[3]Section 507(a) of the Bankruptcy Code provides, in pertinent part:

> (a) The following expenses and claims have priority in the following order:
>
> (1) First, administrative expenses allowed under section 503(b) of this title
>
> . . . .

Code does not provide any explicit definition of "incurred," the reference in Section 503(b)(1)(B)(i) to Section 507(a)(7) strongly suggests that property taxes should be considered "incurred" when they are assessed. The lower courts' interpretation of Sections 503 and 507 precludes a property tax such as that at issue here from being treated as an administrative expense because it was purportedly *"incurred"* before the commencement of the case and yet also ousted it from seventh priority status because it was "assessed" after commencement of the case.

The obvious solution to this anomaly is to treat the words "incurred" and "assessed" as synonymous in the context of property taxes. The reason that the term "assessed" is not used in Section 503, while it *is* used in Section 507, is that Section 503 applies to "any tax," while Section 507(a)(7)(B) applies only to "a property tax." Taxes other than property taxes may be "incurred" without being "assessed," and so the more general term must be used in Section 503.

As one commentator on bankruptcy matters has stated, "the pre- versus post-petition status of a property tax claim is determined by the date of assessment, rather than the date the tax becomes delinquent." Kenneth A. Hill, *Treatment of Interest and Penalties on Tax Claims in Chapter 11 Bankruptcy Cases,* 1994-95 Annual Survey of Bankruptcy

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(7) Seventh, allowed unsecured claims of governmental units, only to the extent that such claims are for --

(B) a property tax assessed before the commencement of the case and last payable without penalty after one year before the date of the filing of the petition.

Law, p. 177, 181. "Reliance on the assessment date is a feature unique to property tax claims." *Id.* at 178, note 1.

Other sections of the Bankruptcy Code also recognize that, for property tax purposes, the date of assessment is key. For example, assessment of a property tax is not barred by the automatic stay provided by Section 362(a) of the Bankruptcy Code. *Id.* at 179.

B. The Third Circuit's Decision Fails To Recognize The Unique Nature Of Property Taxes In Bankruptcy.

Resolution of the issue in this case requires an understanding of the unique nature of property taxes. Income taxes, payroll taxes, or sales taxes are based upon activities which occur throughout the tax year. Such tax liabilities are determined and remitted as the year progresses. Furthermore, income taxes, payroll taxes, sales taxes and the like can be self-assessed through the application by the taxpayer of a pre-set tax rate to the taxable transaction to determine liability. These tax liabilities are attributable to discrete events which directly determine the tax liability.

A property tax liability, however, is not based on a discrete event, but is typically a function of a levy rate, redetermined annually, applied against the value of the taxpayer's property as of some arbitrary date preceding the tax year. The taxes at issue in this case were levied in 1992 based on a 1991 assessed valuation of property owned by the taxpayer as of December 31, 1990.

In West Virginia, property taxes are not self-assessed. A property tax return such as that filed by the Debtor on May 1, 1991, is not like an income tax return on which the taxpayer calculates its tax liability; rather, a property tax return merely lists the property to be assessed. Until that property is valued (appraised) by the assessing authority (in this case, the BPW), no tax can be calculated. This

procedure is markedly different than income taxes, gross-receipts taxes, or sales taxes, which taxes can be calculated by applying a statutorily pre-determined tax rate against the taxable event.

Indeed, even after the value has been "assessed" no tax can be calculated because the tax levying bodies (counties, cities, and school districts) must levy the tax, an event which cannot take place until *after* the Board of Public Works has determined, by "assessment," the value of the property.[4] These local tax-levying bodies did not fix their levy rates until March and April of the tax year (1992) *after* they had received the total assessed value of the property, including that at issue here. (The levying bodies cannot calculate the tax rate necessary to raise sufficient revenues until they know the value of the tax base.) *See*, W. Va. Code §§ 11-6-13, 11-6-14, 11-6-16, 11-8-8, 11-8-9, 11-8-10, and 11-8-12 (Appendix F).

The taxing authority does not know what property is located in its jurisdiction until the informational tax return is filed. The BPW must then determine the value of the property to be taxed and the levying bodies must determine tax rate. Only then can the tax liability be calculated from those two factors.

Depending on circumstances, there may not be any property tax liability for a certain taxpayer, or for certain classes of property, in a given year; but that determination cannot be made until well into the assessment process. *See Forsyth County v. Burns, (unpublished)* 21 C.B.C.2d 1337, 1342 n.3 (4th Cir. 1989) *reh'g en banc denied*, 1990 U.S.

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[4]The BPW is only one of several taxing authorities for purposes of the public utility property tax. The BPW centrally assesses the *value* of the property held by public utilities, but the local jurisdictions each year set their own tax levy rates to be applied to the assessment, and the tax bills are then calculated and sent to the taxpayer by the State Auditor. W. Va. Code §§ 11-6-14 and 11-6-16. About two-thirds of the tax revenue from property taxes is levied by local county school districts.

App. Lexis 7381 (4th Cir. 1990) ("in the euphoria of what formerly were seemingly unlimited revenues flowing from local taxation on oil and gas extraction, certain of the Louisiana parishes could well have concluded that local taxpayers should have no obligation for taxes for a given year, and the parish governing bodies in that case could have set a zero tax rate for that particular year"). No tax liability can truly be said to exist until the assessment is complete.

The lower courts failed to recognize the factually unique nature of property taxes, and the opinion of the Third Circuit panel ignored West Virginia's argument that property taxes are therefore uniquely treated under the Bankruptcy Code. In ignoring this argument, the Third Circuit panel has interpreted the Bankruptcy Code to reach an incongruous result -- property taxes for the 1990 and 1991 tax years are allowed a seventh priority under Section 507(a)(7)(B) because they are "assessed before the commencement of the case and last payable without penalty after one year before the date of the filing of the petition", and property taxes for the 1993 tax year receive a first priority as administrative expenses because they are "incurred by the estate", but property taxes for the 1992 tax year (the taxes at issue in this case) receive no priority at all.

Because the 1992 taxes were assessed *after* the filing of the petition and yet were "incurred" (according to the Third Circuit panel) prior to the filing of the petition, the decision of the Third Circuit panel removed the 1992 taxes from all subsections granting priority to state taxes. This result is internally inconsistent and clearly at odds with the intent of Congress to treat taxes favorably under the Bankruptcy Code.

II. DECISIONS ADDRESSING WHEN A PROPERTY TAX IS "INCURRED" ARE IN CONFLICT.

A. The Result Below Conflicts With A Fourth Circuit Decision And Other Courts Addressing The Same Issue.

Cases which have addressed the precise issue in this case have held that property taxes are incurred upon assessment. *See, e.g., Forsyth County v. Burns, (unpublished)* 21 C.B.C.2d 1337 (4th Cir. 1989), *rehearing en banc denied,* 1990 U.S. App. Lexis 7381 (4th Cir. 1990); (property taxes levied post-petition based on pre-petition status date were administrative expenses); *In re Pioneer Title Building, Ltd.,* 133 B.R. 822 (Bankr. W.D. Tex. 1991) (property taxes which were assessed post-petition while the debtor-in-possession owned and operated the property were administrative expenses); *In re Fairchild Aircraft Corp.,* 124 B.R. 488 (Bankr. W.D. Tex. 1991) (property taxes assessed post-petition are obligations of the estate, regardless of whether the property was valued "as of" a date prior to commencement of the case); *cf. In re R.H. Macy & Co.,* 157 B.R. 548 (S.D.N.Y. 1993) (personal property tax was not incurred on the pre-petition status date, but rather on the post-petition "tax-due" date).

The cases relied upon by the lower courts and the IRS are easily distinguishable because, while they treat the "status date" as the date the tax was "incurred," the relevant state statutes provided for a lien to attach on the tax status date. *See In re Members Warehouse, Inc.,* 991 F.2d 116 (4th Cir. 1993), *In re Point Restaurant and Oyster Bar,* 86 B.R. 252 (Bankr. N.D. Fla. 1988). These cases treated the "lien date" as a significant factor in their determination. Unlike the state statutes involved in those cases, in West Virginia a lien for property taxes does not attach until December 31 of the assessment year, one full year after the status date.

Emphasizing the frequency with which the issue of the priority status of property taxes in bankruptcy arises, in addition to this Petition For Writ of Certiorari, this Court has also recently received a petition from a decision of the Fifth Circuit in a similar case. *See Midland Central Appraisal District v. Midland Industrial Service Corporation,* No. 94-1235, filed December 27, 1994. In *Midland,* the Fifth Circuit held that "[t]he Taxes are not administrative expenses of the estate because the events which triggered the tax liability, ownership of the property *and attachment of the tax lien,* occurred pre-petition. *MCAD is not entitled to assert both a pre-petition secured tax lien and a post-petition administrative expense for the same tax."* 35 F.3d 164, 167 5th Cir. 1994) (emphasis added, footnote omitted).

West Virginia's position in this case is stronger than that of the petitioner in *Midland,* and provides a clearer illustration of the need to read Section 503 together with Section 507. The Texas law applied in *Midland* provides for a lien to attach on the status date, which clearly influenced the Fifth Circuit's decision, while West Virginia law does not provide for attachment of a lien until a year after the status date. Whereas the taxing authority in *Midland* is in a similar situation as the taxing authorities in *Point Restaurant and Oyster Bar, supra,* and *Members Warehouse, supra,* this case presents the Court with a unique situation among the current circuit court decisions because the taxes at issue in this case do not enjoy secured status. Unlike the petitioner in *Midland,* West Virginia is not attempting to be awarded "both a pre-petition secured tax lien and a post-petition administrative expense for the same tax." Thus, the impact of the "no priority" gap between the seventh priority of Section 507(a)(7)(B) and the administrative expense priority of Section 503(b)(1)(B)(i) is felt especially strongly by taxing

jurisdictions such as West Virginia, which do not have the benefit of a pre-petition lien.[5]

B. The Decision Below Conflicts With The Reasoning Of The Third Circuit On A Related Issue.

Furthermore, the decision by the Third Circuit in this case is inconsistent with another Third Circuit decision which addressed the relative importance of the tax status date and the assessment date when dealing with property taxes in bankruptcy. In *Makoroff v. City of Lockport,* 916 F.2d 890 (3d Cir. 1990), *cert. denied, City of Lockport v. United States,* 499 U.S. 983, 111 S. Ct. 1640, 113 L. Ed. 2d 735 (1991), the Third Circuit considered the case of a post-petition assessment based upon a pre-petition valuation date (or "status date"), and whether the automatic stay barred local taxing authorities from perfecting a lien on the subject property. The decision in *Makoroff* hinged on whether the local taxing authorities had an "interest in property" as required to fall within the exception to the automatic stay provided by § 546(b) of the Bankruptcy Code. In holding that the local New York taxing authorities did not acquire an "interest in property" on the tax status date, the panel in *Makoroff* set forth the following reasoning:

> The tax status date merely represents a date when the identity of the taxpayer and the value of the property are established. . . . We believe that the tax status date is an arbitrary date chosen solely for

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[5]The automatic stay provisions of Section 362(a) of the Bankruptcy Code prevent the creation of a lien on a tax that was assessed post-petition. *Equibank, N.A. v. Wheeling-Pittsburgh Steel Corporation,* 884 F.2d 80, 85-86 (3d Cir. 1989). Thus, property taxes like those at issue in this case, which are assessed post-petition but to which a lien has not attached pre-petition, do not receive any priority (according to the Third Circuit panel in this case), and are also prohibited from ever becoming secured claims.

> ease in tax administration. Immediately following that date, the taxing entity still possessed no more than an expectation that taxes will be collected with respect to a particular property. . . . Calling such an expectation an "interest in property" *before the amount of the tax is established and a perfectible lien created,* stretches the scope of that phrase beyond its commonly understood meaning.

Makoroff, 916 F.2d at 895-96 (emphasis added, citations omitted).

Thus, an apparent conflict exists regarding the importance of a property tax status date. The Third Circuit's decision in this case holds that a property tax is "incurred" on the tax status date, and yet the court in *Makoroff* held that the tax status date establishes nothing more than "an expectation that taxes will be collected with respect to a particular property", which expectation does not constitute an "interest in property". This apparent conflict illustrates why the opinion of this Court is needed to settle the constantly recurring issue of the significance of a property tax status date in the context of bankruptcy.

C. The Remaining Decisions Relied Upon By The Lower Courts Do Not Address Property Taxes At All.

Other cases relied upon by the lower courts and the IRS are easily distinguishable because they do not deal with property taxes at all, and the opinion of the Third Circuit failed to address the unique nature of property taxes in bankruptcy. After noting that the split among bankruptcy cases dealing with the priority status of property taxes depended on whether a lien attached pre-petition (and also noting that a lien did not attach to the taxes in this case until post-petition), the Third Circuit's opinion inexplicably abandons this discussion and proceeds to draw guidance from cases which addressed when a non-property tax was incurred.

37 F.3d at 985-86. (Appendix B, p. 10). These cases dealing with the priority status in bankruptcy of non-property taxes are completely irrelevant to determining the priority status of a property tax, because the Bankruptcy Code explicitly carves out property taxes as unique and clearly indicates that a property tax is incurred when it is assessed.

CONCLUSION

The priority status accorded to property taxes in bankruptcy proceedings is a continuing source of great concern to state and local government, and will continue to result in litigation until this Court clarifies what congress manifestly intended, that a property tax is "incurred" for purposes of determining its priority status in bankruptcy when it is assessed. The taxes at issue in this case are entitled to administrative expense priority, and should be remitted to the local governments which depend on them.

Respectfully submitted,

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January 25, 1995

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NOS. 93-7532

In re: Columbia Gas Transmission Corporation
Columbia Gas Systems, Inc.,
Debtor

v.

West Virginia State Department of Tax and Revenue

v.

Internal Revenue Service

SUR PETITION FOR REHEARING

Present: SLOVITER, Chief Judge, BECKER, STAPLETON, MANSMANN, HUTCHINSON, SCIRICA, COWEN, NYGAARD, ALITO, ROTH, LEWIS, McKEE, Circuit Judges, and PARELL*, District Judge

The petition for rehearing filed by Appellant West Virginia State Department of Tax and Revenue in the above-entitled case having been submitted to the judges who participated in the decision of this court and to all the other available circuit judges of the circuit in regular active service,

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*Hon. Mary Little Parell, United States District Judge for the District of New Jersey, as to to panel rehearing only.

and no judge who concurred in the decision having asked for rehearing, and a majority of the circuit judges of the circuit in regular active services not having voted for rehearing by the court in banc, the petition for rehearing is denied.

By the Court,

/s/ J. Sloviter
Chief Judge

Dated: Oct 28 1994

Filed October 5, 1994
UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NOS. 93-7531 and 93-7532
(Consolidated)

IN RE: COLUMBIA GAS TRANSMISSION CORPORATION
and COLUMBIA GAS SYSTEMS, INC.,
Debtors

WEST VIRGINIA STATE DEPARTMENT OF
TAX & REVENUE

v.

INTERNAL REVENUE SERVICE

THOMAS E. ROSS,
Trustee
(D.C. No. 92-564)

IN RE: COLUMBIA GAS TRANSMISSION CORPORATION
COLUMBIA GAS SYSTEMS, INC.,
Debtors

THOMAS E. ROSS,
Trustee
(D.C. No. 92-565)

West Virginia State Department of Tax and Revenue,
Appellant in No. 93-7532

Columbia Gas Transmission Corporation ("TCO")
Appellant in No. 93-7531

ON APPEAL FROM THE UNITED STATES
DISTRICT COURT FOR THE DISTRICT OF DELAWARE
(D.C. Nos. 92-564/5)

Argued: March 2, 1994
Before: SLOVITER, *Chief Judge,* ALITO, *Circuit Judge,* and PARELL, *District Judge*[1]

(Opinion Filed: October 5, 1994)

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[1]Hon. Mary Little Parell, United States District Judge for the District of New Jersey, sitting by designation.

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OPINION OF THE COURT

PARRELL, DISTRICT JUDGE.

I.

This appeal originates from an order of the bankruptcy court that denied the motion of Chapter 11 debtor Columbia Gas Transmission Corporation ("Columbia Gas") for

authorization to pay as administrative expenses certain personal property taxes assessed by the State of West Virginia. The district court affirmed that order. We must decide whether certain West Virginia personal property tax liabilities that were based on the ownership of property at a time before the filing of a bankruptcy petition, and were assessed after the filing of the bankruptcy petition, are entitled to priority under the Bankruptcy Code as administrative expenses.

II.

As required under West Virginia law, Columbia Gas filed, on or before May 1, 1991, a tax return with the West Virginia Board of Public Works ("BPW") and reported its property and value of its property within the State of West Virginia as of December 31, 1990. On July 31, 1991, Columbia Gas filed a petition in bankruptcy under Chapter 11 of the Bankruptcy Code, 11 U.S.C. §§ 101, *et seq.* On September 15, 1991, BPW issued Columbia Gas a tentative assessment of its property for purposes of a public service business tax (hereinafter referred to as the "property taxes"), and BPW issued a final assessment on October 15, 1991.

Columbia Gas filed a motion in the bankruptcy court on February 14, 1992 for an order authorizing payment, *inter alia,* of the property taxes as post-petition priority administrative expenses under the Bankruptcy Code, 11 U.S.C. § 503(b)(1)(B). The Internal Revenue Service, which had filed a claim in the proceeding, objected to the motion. The bankruptcy court denied the motion finding that the obligation of Columbia Gas to pay the taxes arose when it owned and operated property in 1990, prior to the filing of its petition. *In re Columbia Gas System, Inc.*, 146 B.R. 114 (Bankr. D. Del. 1992). The district court similarly found that Columbia Gas, and not the bankruptcy estate, incurred the property taxes as a result of owning the property during 1990. The district court accordingly affirmed the order of the bankruptcy court.

On appeal, Columbia Gas and the West Virginia Department of Tax and Revenue contend that the district court and bankruptcy court erred in concluding that Columbia Gas incurred the property taxes pre-petition. They submit that the property taxes were incurred post-petition by the bankruptcy estate because the bankruptcy petition was filed on July 31, 1991, and the tentative assessment was made on September 15, 1991. Appellee, the Internal Revenue Service, argues that the property taxes were incurred pre-petition based on Columbia Gas's ownership of property in West Virginia before December 31, 1990, the date as of which Columbia Gas's property was valued by the West Virginia tax authorities.

III.

We exercise appellate jurisdiction pursuant to 28 U.S.C. § 1291 and 28 U.S.C. § 158(d). This case was decided on stipulated facts. We apply like the district court a plenary standard to legal issues. *See, e.g., Meridan Bank v. Alten,* 958 F.2d 1226, 1229 (3d Cir. 1992).

IV.

The Bankruptcy Code establishes a priority scale by which payments from the bankruptcy estate are made. 11 U.S.C. § 507. Section 507(a)(1) gives first priority to administrative expenses allowable under section 503(b). Section 503(b)(1)(B)(1) of the Bankruptcy Code provides:

> (b) After notice and a hearing, there shall be allowed administrative expenses, other than claims allowed under section 502(f) of this title, including -
>
> . . . .

(1)(B) any tax--

> (1) Incurred by the estate, except a tax of a kind specified in section 507(a)(7) of this title. . . .[1]

11 U.S.C. § 503. The priority for taxes "incurred by the estate" extends only to taxes "incurred" postpetition. *See, e.g.*, 11 U.S.C. § 541(a); *United States v. Friendship College, Inc.*, 737 F.2d 430, 432 (4th Cir. 1984).

Whether or not Columbia Gas is entitled to administrative expense priority for the property taxes depends on which date it "incurred" the property taxes under § 503(b)(1)(B). *See* 3 Collier on Bankruptcy, ¶ 503.04, at 503-34 (15th ed. 1994) ("Whether a tax has been 'incurred by the estate' is not always easy to determine. The time of assessment or payment may not be equivalent to the time the

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[1]Section 507(a) of the Bankruptcy Code provides in pertinent part:

> (a) The following expenses and claims have priority in the following order:
>
> (1) First, administrative expenses allowed under section 503(b) of this title. . . .
>
> . . . .
>
> (7) Seventh, allowed unsecured claims of governmental units, only to the extent that such claims are for -
>
> . . . .
>
> (B) a property tax assessed before commencement of the case and last payable without penalty after one year before the date of the filing of the petition.

Since the Taxes at issue here had not been assessed at the time of the TCO filed its petition in bankruptcy, it is undisputed that the Taxes are not a priority tax under section 507(a)(7).

tax is incurred for the purpose of establishing priority under section 503(b)(1)(B). Rather, the significant fact may be the date the tax accrues.") If the property taxes were "incurred by the estate" of Columbia Gas on September 15, 1991, the date of the tentative assessment, the property taxes must be given priority as an administrative expense under section 503. If, however, before Columbia Gas filed its bankruptcy petition the property taxes were incurred in 1990, the period covered by its May 1, 1991 tax return, the property taxes would not be entitled to administrative priority under section 503(b)(1)(B).

The Bankruptcy Code does not precisely define when a property tax obligation is "incurred."[2] The determination when a state tax is incurred is governed by state law. *See generally Butner v. United States,* 440 U.S. 48, 55, 99 S. Ct. 914, 918, 59 L.Ed.2d 136 (1979); *Arkansas Corp. Comm'n v. Thompson,* 313 U.S. 132, 142, 61 S. Ct. 888, 891, 85 L.Ed. 1244 (1941). The personal property tax obligation in this matter is governed by West Virginia law.

The West Virginia tax assessed against Columbia Gas is a tax assessed by that State against public service businesses. A public service business must file a return with the BPW on May 1 in each assessment year based on the value of property held within West Virginia as of the year ending on December 31 of the year next preceding. *See* W. Va. Code § 11-6-1(a) and (e). Under West Virginia law, by filing this return, ownership of the property is fixed, so that the owner of the property on that date will be charged with the taxes to

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[2]The legislative history does not clearly set forth when a property tax is incurred. Proposed section 346(a), a provision that was not included in the Bankruptcy Code, merely states that "a tax on or measured by . . . use of property . . . or other transaction or events shall be considered incurred on the date of such transaction or event." S. 2266, Calendar No. 1026, Reprinted in *Collier on Bankruptcy,* Appendix Volume 3, pp. VII-344 to VII-345 (15th ed. 1993); *See also,* 124 Cong. Res. 34016 (Oct. 5, 1978 (Sen. DeConcini (enacted Bankruptcy Code adopted substance of definition in section 346(a)).

be assessed thereon, even though the assessment occurs at a later date. *See* 1981 Op. Atty Gen. W. Va. 94, 1981 W. Va. AG LEXIS 23 at *19-23 (March 23, 1981) (transferor liable for public utility taxes on property owned by transferor on December 31, 1975 which were assessed in 1976 notwithstanding transfer of subject property prior to assessment); *see also Cole v. State,* 80 S.E. 487, 491, 73 W. Va. 410, 419 (W. Va. 1913) (real property devoted to religious purposes found tax exempt because "the policy of our law . . . is to have a fixed and definite date by reference to which all property shall be assessed for taxation, and he is the owner for the purpose of taxation who on that day, by himself or his tenant, has the freehold in possession."); *accord Moore v. Johnson Service Co.,* 219 S.E.2d 315, 319, 158 W. Va. 808, 813 (W. Va. 1975) ("in this State, all non-utility property is 'assessed' as of one particular day, . . . even though the actual mechanics of the assessment procedure are likely to occur subsequent to that date."); *George F. Hazelwood Co., v. Pitsenbarger,* 141 S.E.2d 314, 318, 149 W. Va. 485, 490 (W. Va. 1965), *appeal dismissed,* 382 U.S. 201 (1965) (personal property that is located within West Virginia may "be assessed on any day fixed by the Legislature and the tax is determined thereby, even though the property is removed from the state before the tax is due or even before the assessor actually entered his figures.")

The BPW issues such a tentative assessment on or before September 15, and final a assessment not later than October 1. *Id.* §§ 11-6-9, 11-6-10, and 11-6-11. After such assessment is completed, one-half the taxes are due in the following September, and one-half are due in the following March. *Id.* § 11-6-18. A lien on the property of a public service business attaches on December 31 of the assessment year. *Id.* § 11-6-23.

Here, as required under West Virginia law, Columbia Gas filed, on or before May 1, 1991, a tax return covering the year ended December 31, 1990. Columbia Gas subsequently filed a bankruptcy petition on July 31, 1991. The public service business property tax was thereafter

tentatively assessed against Columbia Gas in September 1991, and finally assessed against Columbia Gas in October 1991, based on the value of property held by Columbia Gas within West Virginia as of December 31, 1990. A lien arose as of December 31, 1991. Half of the property taxes at issue was due in September 1992, and the other half was due in March 1993.

Several cases have held that property taxes are incurred upon assessment. *See, e.g. Forsyth County v. Burns,* 21 C.B.C.2d 1337 (4th Cir. 1989); *In re Pioneer Title Building, Ltd.,* 133 B.R. 822 (Bankr. W.D. Tex. 1991) (ad valorem property taxes assessed postpetition entitled to administrative expenses); *In re Fairchild Aircraft Corp.,* 124 B.R. 488 (Bankr. W. D. Tex. 1991) ("Taxes assessed post-petition are therefore obligations of the estate falling under the express provisions of Section 503(b)(1)(B)"); *cf. In re R.H. Macy & Co.,* 157 B.R. 548 (S.D.N.Y. 1993) (personal real estate tax liability was not "incurred" prepetition on the tax status date, but rather was incurred postpetition on the tax due date). On the other hand, where, unlike in this matter, a lien attaches under state law to the taxed property before the bankruptcy petition is filed, courts have held that a post-petition assessment or setting of the relevant tax rate does not make the taxes administrative expenses incurred by the estate. *See In re Point Restaurant and Oyster Bar,* 86 B.R. 252 (Bankr. N.D. Fla. 1988), (Florida statutory scheme imposed lien on taxable personal property as of prepetition date of its valuation despite fact that determination of actual tax not made until after bankruptcy petition filed); *cf. In re Members Warehouse, Inc.,* 991 F.2d 116 (4th Cir. 1993) (determining debtor's liability for the payment of North Carolina ad valorem property taxes where lien attached to property on the date of listing of property.)

While this case involves a property tax liability, in other contexts a tax liability is generally "incurred on the date it accrues, not on the date of the assessment or the date on which it is payable." *In re Bondi's Valu-King, Inc.* 102 B.R. 108, 110 (Bankr. N.D. Ohio 1989) (citation omitted), *aff'd on*

other grounds, 126 B.R. 47 (N.D. Ohio 1991) (federal unemployment taxes); *see In re Connecticut Motor Lines, Inc.,* 336 F.2d 96 (3d Cir. 1964) (Pre-code case dealing with federal taxes arising from wages); *see also Otte v. United States,* 419 U.S. 43, 95 S. Ct. 247, 42 L.Ed.2d 212 (1974) (withholding taxes); *In re Prime Motor Inns, Inc.,* 144 B.R. 554, 555 (Bankr. S.D. Fla. 1992) (Income tax based on pre-petition sales of assets was not administrative expense; "a tax accrues on the date it *is incurred,* not the date of the assessment or the date it is payable." (emphasis in original)); *In re O.P.M. Leasing Services, Inc.,* 68 B.R. 979, 983-985 (Bankr. S.D.N.Y. 1987) (income tax liability attributable to pre-petition portion of debtor's fiscal year, determined and paid post petition, was not administrative expense).

In *Connecticut Motor Lines,* a case decided under the Bankruptcy Act of 1898, § 64a, 11 U.S.C. § 104(a)(1) (1976 ed.), this Court found that taxes arising from wages relating to services rendered prior to the bankruptcy, but paid during the bankruptcy, were not entitled to priority as an administrative expense. This Court reasoned, among other things, that

> the employer, in a case in which he was not involved in a bankruptcy proceeding, would have had to pay the wages as employer, under the Internal Revenue Code, even if he were no longer, in actuality, employer. And he would, at the time of payment, have had to pay the accrued taxes, despite his no longer being employer.

336 F.2d at 106, *see also Dewsnup v. Timm,* 112 S.Ct. 773, 779, 116 L.Ed.2d 903 (1992) (courts generally reluctant to assume Congress intended to effect major change in Pre-Code practice in absence of clear indication to contrary).

Here similarly, the taxes were incurred on the date that the property was owned by Columbia Gas as indicated in its May 1, 1991 tax return covering the year ended December 31, 1990. It would not have affected the tax liability of

Columbia Gas under West Virginia law if its property in West Virginia had been sold or destroyed after the ownership of the property in 1990 had fixed lability.

The ownership of the property in 1990, the event giving rise to the property tax, like the taxes arising from wages in *Connecticut Motor Lines*, occurred before the petition for bankruptcy had been filed. Based on West Virginia law, we conclude that the property taxes were incurred pre-petition, even though the amount of tax had not yet been determined. Accordingly, the property taxes are not entitled to administrative expenses under section 503(b)(1)(B)(i), and the order of the district court will be affirmed.

A True Copy:
Teste:

Clerk of the United States Court of Appeals
for the Third Circuit

C-1

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF DELAWARE

In Re

THE COLUMBIA GAS SYSTEM, INC, and COLUMBIA GAS TRANSMISSION CORPORATION,

C.A. Nos. 92-564-SLR
92-565-SLR

(Bankruptcy Nos. 91-803, 91-804)

Debtors,

WEST VIRGINIA STATE DEPARTMENT OF TAX AND REVENUE,

Appellants,

v.

C.A. No. 92-564-SLR

INTERNAL REVENUE SERVICE,

Appellee,

ORDER

At Wilmington this 23rd day of June, 1993 for the reasons set forth in the Court's Memorandum Opinion entered in this case on this date, it is

HEREBY ORDERED:

The Order of the Bankruptcy Court of August 19, 1992 in Case No. 91-803 and Case No. 91-804, is hereby affirmed.

Date: June 23, 1993

/s/ Sue L. Robinson
United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF DELAWARE

In Re

THE COLUMBIA GAS SYSTEM, INC, and COLUMBIA GAS TRANSMISSION CORPORATION,

C.A. Nos. 92-564-SLR
92-565-SLR
(Bankruptcy Nos. 91-803, 91-804)

Debtors,

WEST VIRGINIA STATE DEPARTMENT OF TAX AND REVENUE,

Appellants,

v.

C.A. No. 92-564-SLR

INTERNAL REVENUE SERVICE,

Appellee,

COLUMBIA GAS TRANSMISSION CORPORATION,

Appellant,

v.

C.A. No. 92-565-SLR

COLUMBIA GAS TRANSMISSION CORPORATION,

Appellee.

Joseph P. Hurley, Esquire, Office of the Attorney General, Wilmington, Delaware, and Robert Weinberger, Esquire, West Virginia State Department of Tax and Revenue, Charleston, West Virginia, of counsel, for appellant, West Virginia State Department of Tax and Revenue.

Robert S. Brady, Esquire, Young, Conaway, Stargatt & Taylor, Wilmington, Delaware, and Robin S. Keller, Esquire, and Laurence Greenwald, Esquire, Stroock & Stroock & Lavan, New York, New York, and John Beerbower, Esquire, Cravath, Swaine & Moore, New York, New York, for appellant Columbia Gas Transmission Corporation.

Ellen Slights, Esquire, Assistant United States Attorney, Wilmington, Delaware, and Stuart D. Gibson, Esquire, Assistant United States Attorney, Washington, D.C., for appellee, Internal Revenue Service.

MEMORANDUM OPINION

Wilmington, Delaware
June 23, 1993

/s/ Sue L. Robinson
Robinson, District Judge

I. INTRODUCTION

In this appeal from the United States Bankruptcy Court for the District of Delaware, the sole issue is whether certain personal property taxes assessed by the State of West Virginia were incurred by Columbia Gas Transmission Corp. ("Columbia Gas") before or after it filed its petition for bankruptcy. The bankruptcy court, in denying Columbia Gas' motion for authorization to pay these taxes, held that the taxes were incurred by Columbia Gas prior to filing for

bankruptcy, and rejected the argument that the taxes had been incurred by the estate as post-petition administrative expenses under 11 U.S.C. § 503(b)(1)(B). In the Matter of The Columbia Gas System, Inc. 146 B.R. 114 (Bankr. D. Del. 1992). Columbia Gas and the State of West Virginia have appealed to this Court.[1] For the reasons set out below, the Court will affirm the bankruptcy court's order.

II. FACTS.

The parties stipulated to the following facts. The tax at issue is a personal property tax centrally assessed against Columbia Gas as a "public service business" ("public utility tax"), pursuant to W.Va. Code §§11-6-1, et. seq., for the period variously referred to as the "1992 tax year" or the "1991 assessment year." (C.A. No. 92-564, D.I. 1, Exhibit 3, ¶3) On or before May 1, 1991, Columbia Gas filed a tax return with the West Virginia Board of Public Works ("BPW") and reported its property and the value of its property within West Virginia as of December 31, 1990. (Id. at ¶ 5) Columbia Gas filed its petition for bankruptcy on July 31, 1991. (Id. at ¶ 6) On or about September 15, 1991, the BPW issued a tentative assessment of the public utility tax. (Id. at ¶ 7) On or about October 31, 1991, the BPW issued the final assessment of the public utility tax for Columbia Gas. (Id.) Under West Virginia law, the State's lien for the public utility tax could not arise until December 31, 1991. Id. at ¶ 10 (citing W.Va. Code §11-6-23) Thus, West Virginia does not have a secured pre-petition claim for

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[1]The appellants filed separate appeals which subsequently have been consolidated. The pre-consolidation request of Columbia Gas for oral argument is denied as the Court finds the present record sufficient to render its decision.

the public utility tax. Id.[2] The amount of tax at issue is $6,700,429.33. Id. at ¶11

III. STANDARD OF REVIEW

On an appeal from a bankruptcy court, a district court exercises plenary review over the bankruptcy judge's legal conclusions and reviews that judge's factual findings under the "clearly erroneous" standard. See Sharon Steel Corp. v. National Fuel Gas Distribution Corp., 872 F.2d 36, 38-39 (3d Cir. 1989); Universal Minerals Inc. v. C.A. Hughes & Co., 669 F.2d 98 (3d Cir. 1981). Because this appeal concerns a purely legal issue, this Court exercises plenary review.

IV. DISCUSSION

Under the Bankruptcy Code, administrative expenses "incurred" by the estate receive first priority. See 11 U.S.C. §503(b)(1)(B)[3] and 11 U.S.C. §507(a)(1).[4] Although the

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[2]See 11 U.S.C. §362(a)(4); Makoroff v. City of Lockport, N.Y., 916 F.2d 890 895-96 (3d Cir. 1990), cert. denied sub nom., City of Lockport, N.Y. v. United States, 11 S.Ct. 1640 (1991).

[3]11 U.S.C. §503(b) provides, in pertinent part:

> (b) After notice and a hearing, there shall be allowed administrative expenses . . . including -- . . .
>
> (1)(B) any tax --
> (i) incurred by the estate, except a tax of a kind specified in section 507(a)(7) of this title. . . .

[4]11 U.S.C. §507 provides, in pertinent part:

§507 Priorities.

(a) The following expenses and claims have priority in the following order:

Bankruptcy Code does not define the term "incurred," it is clear that §503(b)(1)(B) is directed at administrative expenses "incurred" after the debtor files the petition for bankruptcy and the "estate" comes into existence. See 11 U.S.C. §541(a).

The question before the Court on appeal is whether the property taxes at issue were incurred before or after Columbia Gas filed its petition for bankruptcy. "Whether a tax has been 'incurred by the estate' is not always easy to determine. The time of assessment or payment may not be equivalent to the time the tax is incurred for the purpose of establishing priority under section 503(b)(1)(B). Rather, the significant fact may be the date the tax accrues." 3 Collier on Bankruptcy, §503.4 (1993). The bankruptcy court properly determined that the question of whether a state tax is incurred by the debtor pre-petition, or by the estate post-petition, is governed by State law. See, Columbia Gas, 146 B.R. at 116; Butner v. United States, 440 U.S. 48, 55 (1979).

The following are the pertinent provisions of the West Virginia tax code, W.Va. Code §11-6-1 provides, in pertinent part:

> (a) On or before the first day of May in each year a return in writing shall be filed with the board of public works: . . .

> (1) First, administrative expenses allowed under section 503(b) of this title . . .
>
> (7) Seventh, allowed unsecured claims of governmental units, only to the extent that such claims are for -- . . .
>
> (B) a property tax assessed before the commencement of the case and last payable without penalty after one year before the date of the filing of the petition.

Because the taxes at issue in the case sub judice were assessed after commencement of the case, §507(a)(7) is not applicable.

> (5) by the owner or operator of every pipeline, wholly or in part within this state, used for the transportation of oil or gas or water, whether such oil or gas or water be owned by such owner or operator or not . . .
>
> (e) The return required by this section of every such owner or operator shall cover the year ending on the thirty-first day of December, next preceding. . . .

Under subsection (e), the return covers the period ending on December 31 of the previous year. Thus, the tax period at issue in this case is calendar year 1990, clearly a pre-petition period.

The assessment procedures, however, take a substantial amount of time. W.Va. Code §11-6-9 provides, in pertinent part:

> (e) The tax commissioner shall arrange, collate and tabulate such returns and all pertinent information and data contained therein . . . and shall on or before the fifteenth day of September, lay such returns and work sheets, together with his recommendations in the form of a tentative assessment of the property of each such owner or operator, before the board of public works. . . .

The tentative assessment for the tax period at issue, calendar year 1990, was not rendered until approximately September 15, 1991, two months after Columbia Gas filed its petition for bankruptcy.

The final assessment could not occur until a short time after the tentative assessment. W.Va. Code §11-6-10 provides, in pertinent part:

> Upon the fifteenth day after giving the notices required by section 9 (§11-6-9) of this article, or as soon thereafter as reasonably

> convenient but not later than the first day of October, the board of public works shall proceed to assess and fix the true and actual value of all property of such owner or operator hereinbefore required to be returned, in each county through which the . . . pipeline of such owner or operator runs, and in which any property to be assessed is located. . . .

The final assessment of the Columbia Gas property was not rendered until October 1991, three months after Columbia Gas filed for bankruptcy. In addition, the taxes for the 1990 period were not due until the following year, with one-half payable without penalty by September 1992, and one-half payable without penalty by March 1993. W.Va. Code §11-6-18.

Courts have taken two different approaches in determining whether state property taxes, which are related to a pre-petition period but are assessed post-petition, are incurred by the estate. The first approach, the approach taken by the appellants, is that the tax is incurred on the date of assessment, reasoning that the tax can not be incurred until the taxing authority determines the tax rate. See Forsyth County v. Burns, 21 Collier Bankr. Cas. 2d 1337 (4th Cir. 1989) (MB), reh'g denied en banc, 1990 U.S. App. Lexis 7381 (1990). In Forsyth, the United States Court of Appeals for the Fourth Circuit held that property taxes in North Carolina are not incurred until either the tax rate is set or the tax is due, and thus such taxes are administrative expenses when the rate is set post-petition, even though the tax was imposed for the year preceding the filing of the petition. 21 Collier Bankr. Cas. 2d at 1343. See also In re Fairchild Aircraft Corp., 124 B.R. 488, 494 (Bankr. W.D. Tex. 1991); Matter of Stroud Wholesale, Inc., 37 B.R. 735, 741 (Bankr. E.D.N.C. 1984). Applying the assessment method in the case sub judice, because Columbia Gas filed for bankruptcy on July 23, 1991, and the assessment was made on September 21, 1991 (at the earliest), the tax was incurred post-petition

and would be treated as an administrative expense under 11 U.S.C. §503(b)(1)(B).

The second approach, the approach taken by the IRS and the bankruptcy court, is that the tax is incurred on the date the liability for the tax accrues, without regard for whether the taxing authority has set the tax rate. See Columbia Gas, 146 B.R. at 118. See also In re Brent Explorations, Inc., 91 B.R. 104 (Bankr. D. Colo. 1988) (two taxes at issue, one for equipment and one for oil production; equipment tax based upon ownership and presence of equipment within state on particular date, which was post-petition, incurred by estate; production tax based upon production in prior year, which was pre-petition, not incurred by estate); In re Davidson Lumber Co., 47 B.R. 597, 598-99 (Bankr. S.D. Fla. 1985) (IRS claim for recapture of debtor's investment tax credit relating to pre-bankruptcy corporate income tax liability is not an administrative expense as it accrued pre-petition); In re Scrap Disposal, Inc., 24 B.R. 178, 180 (Bankr. S.D. Calif. 1982) (personal property tax related to pre-petition period in which a supplemental assessment to correct an earlier erroneous assessment was rendered post-petition - tax incurred by debtor), aff'd, 38 B.R. 765 (9th Cir. 1984).

The rationale for the accrual approach is that the primary consideration in determining whether an expense is an administrative expense of the estate is when the liability for the tax arises. See In re Brent Explorations, Inc., 91 B.R. at 107 ("incident" of taxation on oil production was production in year which was pre-petition). If the liability arises prior to the existence of the estate, notwithstanding that the amount of liability may not yet be known, then the estate has not received any benefit for which it should pay an expense. Cf. Trustees of Amalgamated Insurance Fund v. McFarlin's, 789 F.2d 98, 101 (2d Cir. 1986) (purpose of §503 is to ensure that estate pays expenses "beneficial to the debtor-in-possession in the operation of the business") (quoting In re Mammoth Mart, Inc., 536 F.2d 950, 954 (1st Cir. 1976)).

The Court will affirm the order of the bankruptcy court, finding the accrual theory to be the better reasoned approach. Section 503(b)(1)(B) applies to administrative expenses "incurred by the estate." The West Virginia public utility tax at issue "cover[s] the year ending on the thirty-first day of December" of 1990. W.Va. Code §11-6-1. The debtor, Columbia Gas, and not the bankruptcy estate, possessed the subject property during 1990. Thus, the debtor incurred the tax as a result of owning the property during 1990. That the amount of the tax was unknown at the time the estate came into existence or whether the taxing authority knew that the subject property may be exempted from taxation is irrelevant; the liability had already accrued as a result of the debtor's owning the property in 1990. Had the property been destroyed between January 1, 1991, and July 22, 1991, or had the subject property been sold on or after January 1, 1991, the taxes would still be due from the debtor, the party that owned the property as of December 31, 1990. See 1981 Op. Atty Gen. W.Va. 94, 1981 W. Va. AG LEXIS 23 at *19-23 (March 23, 1981) (transferor liable for public utility taxes on property owned by transferor on December 31, 1975 which were assessed in 1976 notwithstanding transfer of subject property prior to assessment) (citing Moore v. Johnson Service Co., 219 S.E.2d 315 (W. Va. 1975) (real property tax) and Hazelwood Co. v. Assessor, 141 S.E.2d 314 (W.Va.) (personal property tax), appeal dismissed, 382 U.S. 201 (1965)).

The purpose of §503(b)(1)(B) is to allow the estate to continue to function during the pendency of the bankruptcy proceedings. See generally 11 U.S.C. §503 (types of "expenses of preserving the estate" which are listed include wages, salaries, commissions, taxes, etc.); Trustees of Amalgamated Ins. Fund. v. McFarlin's Inc., 789 F.2d 98 (2d Cir. 1986) (purposes of §503 are to "facilitate the efforts of the trustee or debtor in possession to rehabilitate the business for the benefit of all the estate's creditors"); 3 Collier on Bankruptcy §503.01-04. Thus, § 503 gives priority to the expenses necessary for the estate to operate. It was not necessary for the operation of the estate to possess the subject

property during the year 1990 because the estate did not exist until July 23, 1991. To permit payment of taxes relating to a period before the estate existed as an administrative expense of the estate is not only illogical, but also contrary to the clear purpose of §503.

For the foregoing reasons, the Court will affirm the order of the bankruptcy court which denied authorization to pay the public utility tax relating to the year 1990. The Court shall issue an Order consistent with this Memorandum opinion.

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In the Matter of

THE COLUMBIA GAS SYSTEM, INC., COLUMBIA GAS TRANSMISSION CORPORATION,

Case No. 91-803
Case No. 91-804

Debtors.

MEMORANDUM OPINION AND ORDER

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August 19, 1992

Balick, J.

On February 14, 1992, the Columbia Gas Transmission Corporation (TCo), a debtor-in-possession in this court, filed a motion to pay various property tax liabilities in ten states. The Internal Revenue Service objected to the motion. Extensive discussions between TCo and the IRS resulted in consent orders allowing TCo to pay some of the requested property taxes. TCo voluntarily dismissed its motion with respect to other of the property taxes.

Presently still in dispute are certain property tax liabilities in West Virginia. As to these taxes, the IRS disagrees with the position of TCo and West Virginia that the taxes are entitled to priority as an administrative expense. The parties do agree that whether TCo should be able to pay the West Virginia taxes depends solely on the administrative priority issue. TCo requests expedited consideration of this matter, so as to avoid the possible unnecessary payment of interest, as well as the loss of a pre-payment discount. W. Va. Code § 11-6-18 (1986). This is the court's opinion on this core matter. 28 U.S.C. § 157(b)(2)(A), (B) & (O).

I. Facts

A stipulation the parties filed discloses the following facts. The tax at issue is a personal property tax assessed against TCo as a public service business pursuant to W.Va Code §§ 11-6-1 et. seq.. On or before May 1, 1991, TCo filed a tax return with the West Virginia Board of Public Works. TCo filed its Chapter 11 petition in this court on July 31, 1991. On October 31, the Board issued a final assessment of the public utility tax. At issue are $6,700,429.33 in unpaid public utility taxes. Stipulation of Facts, Case No. 91-803, Docket No. 1563, ¶¶ 3, 8, 11.

II. Discussion

A. The issue

Section § 503(b)(1)(B of title 11 states:

> After notice and a hearing, there shall be allowed administrative expenses,..., including--
>
> (1)(B) any tax--
> (i) incurred by the estate, except a tax of a kind specified in section 507(a)(7) of this title.

The parties agree the sole and dispositive legal issue is whether the public utility tax here:

> [I]s a tax "incurred by the estate," within the meaning of 11 U.S.C. § 503(b)(1)(B), and is therefore entitled to priority as an administrative expense.

Stipulation, § 13. TCo's bankruptcy estate came into existence upon the filing of its Chapter 11 petition. TCo asserts the public utility tax was "incurred" post-petition and therefore was incurred "by the estate." The IRS counters that the public utility tax was incurred pre-petition.

B. The parties' arguments

The term "incurred" is not defined by the Bankruptcy Code, and has not been analyzed by any cases within the Third Circuit.[1] The litigants have cited many decisions from

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[1]TCo's suggestion in its brief that Equibank, N.A. v. Wheeling-Pittsburgh Steel Corp., 884 F.2d 80 (3d Cir. 1989) addresses the 503(b) issue and supports its motion is without merit.

courts in other Circuits analyzing whether a state tax was "incurred by the estate." These courts have adopted primarily two different methodologies of determining when a tax obligation is incurred. The litigants characterize these methodologies as the date of accrual rule, and the date of assessment rule. The date of accrual rule (favored by the IRS) holds that the tax obligation is incurred when the tax accrues, or when an incident of taxation arises. The date of assessment rule (favored by TCo) holds that the tax is not incurred until the taxing authority actually assesses the amount of the tax.

The litigants argue this court should adopt one or the other of these respective rules and apply it here. The premise of their arguments is that one rule is appropriate regardless of state law. This premise violates the teachings of Butner v. United States, 440 U.S. 48, 55 (1979) and is incorrect. When a tax obligation arises is a question of state law, and is not governed by the analysis of a different state's tax law. Instead of adopting one of the two methodologies, this court needs to determine the Bankruptcy Code meaning of "incurred" and apply it to the state law at issue here.

C. The Bankruptcy meaning of "incurred"

"Incur" is defined as "become liable or subject to." Websters 3rd New International Dictionary 1146 (16th ed. 1971). The relevant legislative history of section 503(b) states:

> In general, administrative expenses include taxes which the trustee incurs in administering the debtor's estate, including taxes on capital gains from sales of property by the trustee and taxes on income earned by the estate during the case.

S.Rep. No. 989, 95th Cong., 2d Sess. 66 (1978) (emphasis added). The court concludes the legal issue before it should be slightly rephrased in more commonly used terms--whether

TCo's legal obligation, or liability on a claim, to pay the tax first arose before or after the filing date. See 11 U.S.C. § 101(12).

The Third Circuit has already explained how to determine when liability on a claim first arises. In In re Remington Rand Corp., 836 F.2d 825 (3d Cir. 1988), at issue was when the United States first possessed a claim arising under the Contract Dispute Act of 1978. There, the government had not, prior to confirmation of the debtor's plan, completed a certification procedure that was a prerequisite to the government's ability to sue the debtor under the Contract Act. The government argued its claim arose post-confirmation and was thus not discharged.

In considering this argument, the Remington court started with the Bankruptcy Code definition of a claim:

> [A] right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed....

Id. at 829 (quoting 11 U.S.C. § 101(4)(A)). The Remington court then examined the language of the Contract Act. It found that the Act first required the governmental contract officer to find that the government indeed had a valid claim, and that this administrative requirement was a jurisdictional prerequisite to judicial resolution of the claim. 836 B.R. at 830. However, the court found nothing in the Act intending to exclude a claim arising under it from the Bankruptcy Code's broad definition of a claim. The Remington court recognized the legal principle that "a party may have a bankruptcy claim and not possess a cause of action on that claim." Id. at 831-32. The court concluded that the government's claim arose when it knew of the alleged breach--this is when the right to payment arose, even though the claim would at that time be merely contingent and not

fixed, and even though under the Contract Act no judicial jurisdiction yet existed. Id. at 831-33.[2]

TCo and West Virginia rely heavily on the unreported decision of Forsyth County v. Burns, 21 Collier Bankr. Cas. 2d (MB) 1337, (Nov. 24, 1989), reh'g denied en banc, 1990 U.S. App. Lexis 7381 (1990). That court held that North Carolina property taxes are not incurred until either the tax rate is set or the tax is due, because until then, no right to payment exists. This reasoning conflicts with that of Remington and must therefore be rejected.

This court will utilize the Remington court's analysis of a "claim" under the Bankruptcy Code as applied to the body of law that creates the claim at issue here --West Virginia tax law. Specifically, the question is only whether, under West Virginia law, West Virginia's right to payment for the public utility tax arose pre-petition or post-petition.

D. West Virginia Public Utility Tax Law

The public utility tax is an ad valorem tax which is "based upon the value of the property, tangible or intangible." City of Fairmont v. Pitrolo Pontiac-Cadillac Co., 308 S.E.2d 527, 530 (W. Va. 1983). West Virginia law establishes the following chronological procedure for reporting and payment of public utility taxes. TCo must file a tax return by the first of May each year. W. Va. Code § 11-6-1(a)(5) (1986). The return contains detailed information describing the quantity and value of TCo's pipelines and related realty within West

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[2]The IRS has cited several cases that utilize a similar analysis. E.g., In re O.P.M. Leasing Services, Inc., 68 B.R. 979, 983-85 (Bankr. S.D.N.Y. 1987); In re Ames Dept. Stores, 136 B.R. 353, 356 (Bankr. S.D.N.Y. 1992). Even the primary case TCo and West Virginia rely upon agrees with this approach. Forsyth County v. Burns, 21 Collier Bankr. Cas. 2d (MB) 1337, 1139 n.2 (Nov. 24, 1989), reh'g denied en banc, 1990 U.S. App. Lexis 7381 (1990).

Virginia that enables the Board to determine the value of TCo's property. § 11-6-5; § 11-6-1(e). As to the year upon which the return is based, "the return...[of TCo] shall cover the year ending on the thirty-first day of December, next preceding...." § 11-6-1(e). While the phrase "next preceding" is hardly unambiguous, the parties do not dispute that here it refers to the prior year. If TCo fails to file a return, the West Virginia Code provides remedies for compelling compliance with § 11-6-1, as well as for criminal sanctions that can be imposed upon TCo. § 11-6-8; § 11-6-9. The tax commissioner examines the return, and notifies the Board and TCo of his tentative assessment by the fifteenth of September. § 11-6-9(e).

Next, not later than the first of October of the year in which the return is filed, the Board "shall proceed to assess and fix the true and actual value of all property of [TCo.]" § 11-6-11. If this assessment and valuation is not appealed, it is "final and conclusive." Id. Finally, the state auditor then serves TCo with a statement of all taxes assessed, and:

> [I]t shall be the duty of [TCo], to pay one half of the amount of such taxes...into the treasury of the State by the first day of September and the remaining one half by the first day of the following March....

§ 11-6-18.

E. The Public Utility Taxes Were No Incurred by the Estate.

As contemplated by these statutes, TCo filed its return as required by May 1, 1991. A tentative assessment was issued by September 15, 1991. On October 31, 1991, the Board determined and notified TCo of the final assessment of the public utility tax. Thus the public utility taxes at issue here were finally determined on approximately October 31, and one-half become due on September 1, 1992.

Upon consideration of this statutory scheme as a whole, the court concludes TCo's obligation to pay the taxes arose when it owned and operated property within the prior calendar year (1990). Nothing in the statute suggests that West Virginia's right to payment is dependent upon the assessment procedure that commences following the filing of its return. The assessment procedure is an administrative procedure for fixing the amount of the tax owed, Western Md. Ry. v. Board of Pub. Works, 90 S.E.2d 438, 445 (1955), and the tax is not "due" until the completion of this process. § 11-6-18. However, as discussed in Remington, this is not required for an unmatured, contingent claim for taxes to exist.

III. Conclusion

The public utility taxes at issue here were incurred by TCo prior to the filing of its petition. An order in accordance with this Memorandum Opinion is attached.

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In the Matter of

THE COLUMBIA GAS SYSTEM, INC., COLUMBIA GAS TRANSMISSION CORPORATION,	Case No. 91-803 Case No. 91-804

Debtors.

ORDER

AND NOW, August 19, 1992, for the reasons stated in the attached Memorandum Opinion,

IT IS ORDERED THAT TCo's motion to pay West Virginia $6,700,429.33 in unpaid public utility taxes as an administrative expense is DENIED.

/s/ Helen S. Balick
JUDGE

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re	Chapter 11
THE COLUMBIA GAS SYSTEM, INC. and COLUMBIA GAS TRANSMISSION CORPORATION,	Case No. 91-803 Case No. 91-804
Debtors	

STIPULATION OF FACTS

Debtor Columbia Gas Transmission Corporation (TCO), The Internal Revenue Service (IRS), and the State of West Virginia (West Virginia) hereby stipulate that the following facts, pertaining to TCO's February 14, 1992 Motion for a Order Authorizing TCO to Pay Certain Pre-Petition Property Tax Liabilities, are true.

1. On or about February 14, 1992, TCO filed a motion for an Order authorizing it to pay property taxes to state and local taxing jurisdictions in ten states: Kentucky, Maryland, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Texas, Virginia and West Virginia. In support of its motion, TCO alleged that the taxes which it then sought authorization to pay constituted either secured pre-petition claims, claims entitled to priority under Code §507(a)(7), or administrative expenses under Code §503(b). The United States, on behalf of its Internal Revenue Service, filed the only objection to TCO's motion.

2. By Consent Orders entered March 18, 1992 and June 11, 1992, the Court authorized TCO to pay certain of the taxes which were the subject of its February 14, 1992

motion. Pursuant to its settlement of those issues with the IRS, TCO withdrew its motion for authorization to pay other taxes which were the subject of that motion.

3. The only tax which TCO sought authorization to pay, and which has not been settled or withdrawn, is the West Virginia personal property tax centrally assessed against TCO as a "public service business," pursuant to W.Va. Code §§11-6-1, et.seq., for the period variously referred to as the "1992 tax year" or the 1991 "assessment year." In this Stipulation, the parties refer to this particular tax as the "public utility tax."

4. Attached to this Stipulation as Joint Exhibit 1-A is a copy of the provisions of the West Virginia Code, as they pertain to this dispute. The particular sections which apply to this dispute are summarized below.

5. On or before May 1, 1991, TCO filed a tax return with the West Virginia Board of Public Works (BPW), reporting its property and the value thereof within the State of West Virginia, as of December 31, 1991. W.Va. Code §11-6-1(a) and (e).

6. TCO filed its petition in bankruptcy in this Court on July 31, 1990.

7. On or about September 15, 1991, the BPW issued the tentative assessment of the public utility tax, a copy of which is attached hereto as Joint Exhibit 2-B, pursuant to W.Va. Code §11-6-9(e).

8. On or about October 31, 1991, the BPW issued the final assessment of the public utility tax, a copy of which is attached hereto as Joint Exhibit 3-C, and gave notice to TCO of that assessment pursuant to W.Va. Code §11-6-11. TCO did not appeal that assessment.

9. One-half of the public utility tax is due and payable on or before September 1, 1992, and the other half

is due and payable on or before March 1, 1993, pursuant to W.Va. Code §11-6-18.

10. Because its lien for the public utility tax did not arise until December 31, 1991 (W.Va. Code §11-6-23), after TCO filed its petition for relief, West Virginia does not have a secured pre-petition claim for the public utility tax.

11. On or about July 15, 1992, West Virginia issued the "Statement of Taxes-1992," a copy of which is attached hereto as Joint Exhibit 4-D, pursuant to W.Va. Code §11-6-18. The parties do not dispute the amount of public utility tax at issue, which totals $6,700,429.33.

12. Attached hereto as Joint Exhibit 5-E are copies of the tentative and final assessments and Statement of Taxes for the period variously referred to as the "1991 Tax Year," or the 1990 "assessment year."

13. This dispute presents the legal issue, whether the public utilities tax which TCO owes to the State of West Virginia for the period variously referred to as the "1992 tax year" or the 1991 "assessment year" is a tax "incurred by the estate," within the meaning of 11 U.S.C. §503(b)(1)(B), and is therefore entitled to priority as an administrative expense. The parties agree that, if the Court answers this question in the affirmative, it should authorize TCO to pay the 1991 West Virginia public utilities tax, in order to avoid the accrual of interest and penalties, which are also entitled to administrative priority. The parties also agree that, if the Court determines that this tax was not "incurred by the estate," it should deny TCO's motion.

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§ 11-6-1. Returns of property to board of public works.

(a) On or before the first day of May in each year a return in writing shall be filed with the board of public works: . . . (5) by the owners or operator of every pipeline, wholly or in part within this state, used for the transportation of oil or gas or water, whether such oil or gas or water be owned by such owner or operator or not, or for the transmission of electrical or other power, or the transmission of steam or heat and power or of articles by pneumatic or other power . . . .

. . . .

(e) The return required by this section of every such owner or operator shall cover the year ending on the thirty-first day of December, next preceding, and shall be made on forms prescribed by the board of public works . . . .

§ 11-6-9. Compelling such return; procuring information and tentative assessment by tax commissioner.

(e) The tax commissioner shall arrange, collate and tabulate such returns and all pertinent information and data contained therein, such further evidence or information as may be required by the tax commissioner of such owner or operator, and all other pertinent evidence, information and data he has been able to procure, upon suitable work sheets, so that they may be conveniently considered, and shall on or before the fifteenth day of September, lay such returns and work sheets, together with his recommendations in the form of a tentative assessment of the property of each such owner or operator, before the board of public works. And as soon as the tax commissioner has completed the preparation of such work sheets and tentative assessments, he shall notify the owner or operator affected thereby of the amount of such tentative assessment by written notice deposited in the United States post office . . . .

§ 11-6-11. Valuation of property by board.

After the fifteenth day after giving the notices required by section nine [§ 11-6-9] of this article, or as soon thereafter as reasonably convenient but not later than the first day of October, the board of public works shall proceed to assess and fix the true and actual value of all property of such owner or operator hereinbefore required to be returned, in each county through which the . . . pipeline of such owner or operator runs, and in which any property to be assessed is located. . . . Before any assessment shall be made by the board, any and all evidence, information and data considered by the board shall be available for inspection by any such owner or operator or his duly authorized representative, and an opportunity given to be heard thereon when the board of public works has assessed any property hereby required to be returned, and has determined the valuation thereof, such assessment and valuation shall be entered of record in the book of minutes of its proceedings, and shall be certified by the secretary of the board to the auditor.

. . . As soon as such assessment is made, the secretary of the board shall notify the owner or operator affected thereby of the amount thereof by written notice deposited in the United States post office, addressed to such owner or operator at the principal office or place of business of such owner or operator. Such assessment and valuation shall be final and conclusive, unless the same be appealed from in the manner following, within fifteen days after such notice is so deposited.

§ 11-6-13 Apportionment of value among counties, districts and municipalities.

In case the list and valuation of the property filed with the tax commissioner be satisfactory to the board of public works, or upon assessment of the property of such owner or operator being made by the board of public works, the

auditor shall immediately apportion to each county, in which any part of such property is situated, the value of the property therein of every such owner or operator as valued or assessed hereunder and the relative value of the total operating property within the state, to be determined upon such factors as the auditor shall deem proper; and further shall apportion such values among the several districts, being school districts, and a proportional valuation to each municipality therein, in which any part of such property is situated, according to the value thereof, as near as may be, and forthwith shall certify to the county commission of such county the values so apportioned. The clerk of the county commission shall forthwith certify such values to the school district and to the several municipalities, respectively, in such county. . . .

§ 11-6-14. Certification of levies to auditor.

The clerk of the county court [county commission] of every county in which any property lies which was so assessed shall, within thirty days after the county and district levies are laid by such court, certify to the auditor the amount levied upon each one hundred dollars' value of the property of each class in the county for county purposes, and on each one hundred dollars of the value of the property of each class in each magisterial district for the district purposes. It shall be the duty of the secretary of the board of education of every school district and independent district in which any part of the property lies, within thirty days after the levies are laid therein for free school and building purposes, or either, to certify to the auditor the amount so levied on each one hundred dollars' value of the property of each class therein for each of such purposes; and it shall be the duty of the recorder, clerk, or other recording officer of every municipal corporation in which any part of the property lies, within the same time, after levies are laid therein for any of the purposes authorized by law, to certify to the auditor the amount levied upon each one hundred

dollars' value of the property of each class therein for each and every purpose.

§ 11-6-16. Entry of assessment by auditor of property of such public service businesses.

As soon as possible after the valuation of the property of such owner or operator is fixed by the board of public works or by the circuit court on appeal as aforesaid, and after he shall have obtained the information herein provided for to enable him to do so, the auditor shall assess and charge each class of property of every such owner or operator with the taxes properly chargeable thereon, in a book to be kept by him for that purpose, as follows: (a) With the whole amount of taxes upon such property for state and state school purposes, if any such taxes are levied; (b) with the whole amount of taxes on such property in each county for county purposes; and (d) with the whole amount of taxes on such property in each municipal corporation for each and all of the purposes for which a levy therein was made by the municipal authorities of such corporation.

§ 11-6-18. Payment of assessment by owner or operator.

The auditor shall, as soon as possible after such assessment is completed, make out and transmit by mail or otherwise, to such owner or operator, a statement of all taxes and levies so charged, and it shall be the duty of such owner or operator, so assessed and charged, to pay one half of the amount of such taxes and levies into the treasury of the State by the first day of September and the remaining one half by the first day of the following March, subject to a deduction of two and one half per centum if the taxes be paid on or before the due date. . . . All moneys received by the auditor under the provisions of this section shall be transmitted to the several counties within twenty days from receipt thereof.

§ 11-6-23. Lien of taxes; notice; collection by suit.

The amount of taxes and levies assessed under this article shall constitute a debt due the State or county, district or municipal corporation entitled thereto, and shall be a lien on all of the property and assets of the taxpayer within the State. The lien shall attach as of the thirty-first day of December following the commencement of the assessment year, and shall be prior to all other liens and charges.

§ 11-8-8. Levies by board of public works; certification.

The state board of public works shall, on or before April fifteenth of each year, levy on the one hundred dollars' valuation of each class of property subject to taxation in the State the rates fixed by section six-a [§11-8-6a] of this article. The board shall forthwith certify its action to the state tax commissioner and to the assessor of each county.

§ 11-8-9. Meetings of local levying bodies.

Each local levying body shall hold a meeting or meetings between the seventh and twenty-eighth days of March for the transaction of business generally and particularly for the business herein required.

§ 11-8-10. Levy estimate by county court [county commission]; certification to tax commissioner and publication.

The county court [county commission] shall, at the session provided for in section nine [§ 11-8-9] of this article, ascertain the fiscal condition of the county, and make an itemized statement setting forth: . . .

(5) The total amount necessary to be raised for each fund by the levy of taxes for the current year;

(6) The proposed county levy in cents on each one hundred dollars' assessed valuation of each class of property for the county and its subdivisions; . . . .

§ 11-8-12. Levy estimate by board of education; certification and publication.

Each board of education shall, at the session provided for in section nine [§ 11-8-9] of this article, if the laying of a levy has been authorized by the voters of the district under article nine [§ 18-91 *et seq.*] of the Code, ascertain the condition of the fiscal affairs of the district, and make a statement setting forth: . . . .

§ 11-8-14. Levy estimate by municipality; certification to tax commissioner and publication.

A municipal governing body shall, at the session provided for in section nine [§ 11-8-9], ascertain the fiscal condition of the corporation and make an itemized statement setting forth:

. . .

(5) The total amount necessary to be raised by the levy of taxes for the current fiscal year;

(6) The proposed rate of levy in cents on each one hundred dollars' assessed valuation of each class of property; and . . . .

Supreme Court, U.S.
FILED
APR 3 1995
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No. 94-1304

In the Supreme Court of the United States

OCTOBER TERM, 1994

WEST VIRGINIA STATE DEPARTMENT OF TAX AND REVENUE, PETITIONER

v.

INTERNAL REVENUE SERVICE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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BEST AVAILABLE COPY

QUESTION PRESENTED

Whether a debt for a West Virginia property tax is "incurred," within the meaning of 11 U.S.C. 503(b)(1)(B), on the date that the liability arises or on the subsequent date that the tax is assessed.

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In the Supreme Court of the United States

OCTOBER TERM, 1994

No. 94-1304

WEST VIRGINIA STATE DEPARTMENT OF TAX AND REVENUE, PETITIONER

v.

INTERNAL REVENUE SERVICE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. B1-B11) is reported at 37 F.3d 982. The opinion of the district court (Pet. App. C1-C11) is not yet reported. The opinion of the bankruptcy court (Pet. App. D1-D8) is reported at 146 B.R. 114.

JURISDICTION

The judgment of the court of appeals was entered on October 5, 1994. A timely petition for rehearing was denied on October 28, 1994 (Pet. App. A1). The petition for a writ of certiorari was filed on January 25, 1995. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. In 1990, Columbia Gas Transmission Corporation owned various pipelines in the State of West Virginia. On or before May 1, 1991, Columbia Gas filed a tax return reporting the value of its pipelines for purposes of the State's public service business property tax for the 1990 tax year (Pet. App. E1).

In July 1991, Columbia Gas filed a petition for relief under Chapter 11 of the Bankruptcy Code (Pet. App. B4). In October 1991, the West Virginia State Board of Public Works notified Columbia Gas of the assessed values of its pipelines in that State for the 1990 tax year (Pet. App. E2). The property tax was thereafter assessed by the State under W. Va. Code § 11-6-16 (Michie 1991).

In February 1992, Columbia Gas filed a motion in its bankruptcy case, seeking an order authorizing payment of the West Virginia property tax as a first priority administrative expense under Sections 503(b)(1)(B) and 507(a)(1) of the Bankruptcy Code. Under Section 507(a)(1) of the Code, "administrative expenses allowed under section 503(b) of this title" are granted first priority. 11 U.S.C. 507(a)(1). In turn, Section 503(b)(1)(B) provides that a tax "incurred by the estate" is an administrative expense unless that tax is separately entitled to seventh priority under the provisions of Section 507(a)(7). See 11 U.S.C. 503(b)(1)(B).[1] The United States, which

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[1] The Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 304(c), 108 Stat. 4132, gave seventh priority to a new category of claims and demoted former seventh priority tax claims to eighth priority. These amendments do not affect this case.

had filed claims in the bankruptcy case, opposed the debtor's motion (Pet. App. E1).[2]

2. The bankruptcy court denied the debtor's motion to treat the property tax as an administrative expense. The court rejected the argument that the obligation to pay the taxes arose only when the taxes were assessed. The court held instead that the tax obligation arose in 1990, before the bankruptcy case commenced, when the debtor owned and operated property in West Virginia. The court held that, because the tax liability was "incurred" within the meaning of Section 503(b)(1)(B) of the Bankruptcy Code by the debtor *before* the bankruptcy case was commenced, the taxes did not represent an administrative expense (Pet. App. D8). The district court affirmed (Pet. App. C1-C11).

3. The court of appeals affirmed (Pet. App. B1-B11). The court noted that a tax must be "incurred" by the estate itself to receive administrative priority (*id.* at B6). Because the Bankruptcy Code does not specify when a state tax is "incurred" for this purpose, the court looked to state law in making this determination (*id.* at B7). The court held that, under the law of West Virginia, a property tax is "incurred" on the date that the property becomes subject to the State's tax (*id.* at B7-B10). In this case, that date was December 31, 1990. After that date, under state law, the debtor's liability for the property tax would not have been altered in any

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[2] In July 1992, the State notified Columbia Gas that the 1990 property taxes levied with respect to its pipelines totaled $6,700,429.33 (Pet. App. E3). One-half of that amount was payable by September 1, 1992; the remainder was payable by March 1, 1993 (Pet. App. E2-E3; see W. Va. Code § 11-6-18 (Michie 1991)).

manner if the pipelines subsequently had been sold or destroyed (*id.* at B10-B11). Because the debtor filed for bankruptcy relief after the date that the property tax liability was thus "incurred," the court held that the tax was not an administrative expense of the estate (*id.* at B11).

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is therefore not warranted.

1. Expenses incurred in administering a bankruptcy estate receive first priority in distributions from the estate. 11 U.S.C. 507(a)(1). Section 503(b)(1)(B) of the Bankruptcy Code generally provides that a tax "incurred by the estate" represents an administrative expense. 11 U.S.C. 503(b)(1)(B). The date on which a tax is "incurred" for this purpose is to be determined under the law of the taxing jurisdiction. See *Arkansas Corporation Commission* v. *Thompson*, 313 U.S. 132, 142 (1941) ("whether or not taxes are 'legally due and owing' to a state depends upon the valid laws of that state").

The court of appeals correctly held that, under West Virginia law, the property tax involved in this case was incurred on December 31, 1990 (Pet. App. B10). That is the date that the debtor's liability for the property tax became fixed. After that date, the debtor's liability for the tax would not have been diminished or in any manner affected if the pipelines subsequently had been sold or destroyed. See *Moore* v. *Johnson Service Co.*, 219 S.E.2d 315, 319 (W. Va. 1975); *George F. Hazelwood Co.* v. *Pitsenbarger*, 141 S.E.2d 314 (W. Va. 1965), appeal dismissed,

382 U.S. 201 (1965); *Cole* v. *State*, 80 S.E. 487 (W. Va. 1913). The property tax liability was therefore "incurred" by Columbia Gas before it filed for bankruptcy relief. Because the property tax was not "incurred" by the estate, it does not qualify as an administrative expense of the estate under Section 503 of the Bankruptcy Code. 11 U.S.C. 503 (b)(1)(B).

The decision of the court of appeals is a direct application of the established principle that a tax is "incurred" when the liability for the tax arises, rather than when it is administratively assessed. For example, this Court's decision in *Otte* v. *United States*, 419 U.S. 43 (1974), involved Section 64a of the Bankruptcy Act of 1898 (the predecessor of Section 503(b) of the Bankruptcy Code), which provided first priority to "the costs and expenses of administration." 11 U.S.C. 104(a)(1) (1976). The Court held in *Otte* that withholding taxes payable after the petition was filed, but with respect to wages paid for services rendered before bankruptcy, were not expenses of administration because the taxes "derive from and are carved out of" the wage claims to which they related. 419 U.S. at 57. See also *In re Connecticut Motor Lines, Inc.*, 336 F.2d 96, 106 (3d Cir. 1964) (denying administrative expense priority to taxes on wages paid for services rendered prior to bankruptcy); *In re Prime Motor Inns, Inc.*, 144 B.R. 554, 555 (Bankr. S.D. Fla. 1992) ("a tax accrues on the date it is incurred, not on the date of assessment or the date it is payable"); *In re Northeastern Ohio General Hospital Ass'n*, 126 B.R. 513, 515 (Bankr. N.D. Ohio 1991) (a tax is not an administrative expense when the "[e]vents upon which the tax is based occurred entirely pre-petition"); *In*

re Wheeling-Pittsburgh Steel Corp., 103 B.R. 672, 693 (W.D. Pa. 1989) (administrative expense status denied "since the transaction or events upon which these taxes are based occurred prepetition"); *In re Bondi's Valu-King, Inc.*, 102 B.R. 108, 110 (Bankr. N.D. Ohio 1989) ("[a] tax is incurred on the date it accrues, not on the date of assessment or the date on which it is payable"), aff'd on other grounds, 126 B.R. 47 (N.D. Ohio 1991); *In re O.P.M. Leasing Services, Inc.*, 68 B.R. 979, 983-985 (Bankr. S.D.N.Y. 1987); *In re Overly-Hautz Co.*, 57 B.R. 932, 937 (Bankr. N.D. Ohio 1986), aff'd on other grounds, 81 B.R. 434 (N.D. Ohio 1987); *In re Davidson Lumber Co.*, 47 B.R. 597 (Bankr. S.D. Fla. 1985); *In re Higgins*, 29 B.R. 196, 201 (Bankr. N.D. Iowa 1983); *In re Melino Cigar & Candy Co.*, 7 C.B.C.2d 71, 73 (Bankr. R.I. 1982).

2. a. Petitioner suggests (Pet. 7-8) that the statutory term "incurred" should be given a meaning with respect to property taxes that differs from its accepted meaning with respect to all other taxes. Although petitioner concedes that other taxes may be "incurred" without being "assessed," petitioner argues (Pet. 7) that the terms "incurred" and "assessed" should be treated as synonymous for property tax purposes.

Congress did not provide that the term "incurred" means "assessed" in one tax context but not in another. When Congress chose to make the priority of a tax turn on the "assessment" date of a tax, rather than on the date it was "incurred," Congress did so expressly. In providing seventh (now eighth) priority for certain types of pre-bankruptcy property taxes, Congress specified that this lower priority would apply to taxes "assessed before the commence-

ment of the case" (11 U.S.C. 507(a)(7)(B)).[3] The suggestion that Congress used the terms "incurred" and "assessed" indiscriminately in referring to property taxes is inconsistent with the plain language of these statutes.

b. Petitioner contends that property taxes should be distinguished from other types of taxes because property taxes are "not based on a discrete event" (Pet. 8) associated with a particular date. Property tax liability, however, is directly attributable to the "event" of ownership of property at the end of a particular year. That is an even more "discrete event" than the "event" of earning income through divers transactions occurring over the course of an entire year.

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[3] Petitioner argues that the use of the term "incurred" in Section 503(b)(1)(B) and "assessed" in Section 507(a)(7)(B) produces a significant anomaly—some property tax claims, such as the claim at issue in this case, will not enjoy either first or seventh priority even though a claim for an older liability may receive seventh priority and a claim for a post-bankruptcy liability may receive first priority (Pet. 6-7). That result, however, is in large part a product of state law, not the Bankruptcy Code. The effect of a delayed assessment is mitigated in some States by statutes providing that a lien arises as of the end of the year when liability is incurred, although the tax is not determined or assessed until a later time. See, *e.g.*, Ohio Rev. Code Ann. § 5727.06(C) (Anderson 1993); N.C. Gen. Stat. § 105-355 (Michie 1994). Even under the present law of West Virginia, the anomaly that petitioner invokes has been largely ameliorated by the Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 401, 108 Stat. 4141, which amends the automatic stay to permit the attachment and perfection of property tax liens after the commencement of the bankruptcy case.

3. The decision in this case is consistent with other appellate decisions. In *Midland Central Appraisal District* v. *Midland Industrial Service Corp.*, 35 F.3d 164 (1994), cert. denied, No. 94-1235 (Mar. 20, 1995), the Fifth Circuit held that a Texas *ad valorem* personal property tax is "incurred" for purposes of Section 503(b)(1)(B) on the date that ownership is determined, for that is "the event that triggers liability." 35 F.3d at 167. Similarly, in *Burns* v. *City of Winston-Salem*, 991 F.2d 116 (1993), the Fourth Circuit held that a North Carolina personal property tax was "incurred" on the date that ownership of the property was determined for purposes of the tax. The court stated that, "[a]lthough the precise amount of the claim was contingent on the tax rate set [on a later date], the contingency would not have affected the tax claim's status as a right to payment." *Id.* at 119 (internal quotation marks omitted).

Petitioner errs in contending (Pet. 11) that the Fourth Circuit's unreported decision in *Forsyth County* v. *Burns*, No. 88-1359 (1989), conflicts with these decisions. In *Burns* v. *City of Winston-Salem*, *supra*, the Fourth Circuit noted that its unpublished decision in *Forsyth County* had no precedential value under that Circuit's Rules. 991 F.2d at 119 n.2. There is thus no conflict among the circuits on the question presented in this case.[4]

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[4] Petitioner asserts that *Makoroff* v. *City of Lockport*, 916 F.2d 890 (1990), cert. denied, 499 U.S. 983 (1991), conflicts with the Third Circuit's decision in the present case. Even if that assertion of an intra-circuit conflict were correct, it would not be an adequate basis for further review by this Court. *Wisniewski* v. *United States*, 353 U.S. 901, 902 (1957).

Petitioner correctly notes (Pet. 11) that the decisions in *Midland Central Appraisal District* v. *Midland Industrial Service Corp.* and *Burns* v. *City of Winston-Salem* involved state taxing schemes under which liens attached on the date that ownership was determined and liability fixed. By contrast, under West Virginia law, the State's lien does not attach until one year after that date. W. Va. Code § 11-6-23 (Michie 1991). That distinction, however, is not material. Administrative expense status under Section 503(b)(1)(B) turns on the date that liability for the tax is "incurred." It does not depend on the date that the taxing authority obtains a lien in the taxpayer's property.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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